



OXFORD ANALYTICA

PERU

FISCAL TRANSPARENCY

Country Report 2005

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PERU



COMPLIANCE RATINGS

<i>Fiscal transparency</i>	<i>2005</i>	<i>2004</i>	<i>2003</i>	<i>2002</i>
Clarity of roles
Availability of information
Budget preparation
Accountability
Score	3.50	3.50	3.25	2.75

OUTLOOK & COMMENTARY

Fiscal transparency has made a number of advances over the past year, though there remains room for further improvement.

Upcoming developments that will further enhance fiscal transparency include the passage of legislation to complement the Law of Fiscal Responsibility and Transparency. This legislation is due to be sent to Congress before the end of the year. Additionally, the law clarifying shared functional responsibilities among different levels of government (LOPE -- *Ley Organica de Poder Ejecutivo*) is currently before Congress. The government is also aiming to issue a plan to devolve certain sectoral responsibilities to regional governments by the end of the year.

There are plans to unify the central government budget formulation system and the Integrated Financial Management System (SIAF). The challenge here is posed by the different classification systems currently used by the two systems.

Weaknesses are likely to remain in the implementation of performance-based budgeting, and no significant progress is expected in the area of privatisation in the near future.

EXECUTIVE SUMMARY

3.50 Enacted

There have been a number of advances over the past year in Peru that have contributed towards building increased fiscal transparency, though there remain several areas with significant room for improvement.

In September 2005, the government issued the regulations implementing the Fiscal Decentralisation Law, which aims at reinforcing prudent budgetary practices of regional and local governments. The regulations aim to, *inter alia*, ensure that the assigning of resources to the regions is carried out in an orderly and gradual manner and they detail various incentives for the regions to use resources efficiently and in a fiscally responsible manner. A pilot programme has been established to foster regional and local government financial management capacity, including the development of multi-annual fiscal frameworks and capacity-building. The law clarifying shared functional responsibilities among different levels of government (LOPE -- *Ley Organica de Poder Ejecutivo*) is currently before Congress. Commentators noted that efforts to replicate the national fiscal system at the local level are hindered by the continuing lack of technical capacity in many of the regions. A referendum took place on 30 October 2005 in which 16 of the 25 departments (regions) voted on whether or not to merge with neighbouring regions to create so-called macro-regions. The merger proposal was overwhelmingly rejected.

Privatisation has stalled over the past year and the government is now primarily restricting itself to operating concessions and conducting a limited number of public-private partnerships (PPPs). The most significant upcoming planned concession is for the Port of Callao, near Lima, though this has been a controversial issue and the timing remains unclear. Commentators noted that there is a need for a clearer definition of what constitutes a PPP and perhaps even a law governing their framework to increase transparency.

Legislation to complement the Law of Fiscal Responsibility and Transparency is due to be sent to Congress before the end of the year. This will aim to strengthen the procedures for compliance, monitoring, and reporting to Congress and the public. Commentators described the law in its current state as lacking ‘teeth’, that is, sanctions for non-compliance.

In June 2005, the General Law on the National System of Public Indebtedness was passed. This aims to provide a stable legal framework to engender a more efficient and orderly administration of public sector debt. It establishes rules on annual limits on debts and guarantees conducted through the central government, as well as on contingent liabilities stemming from concessions and PPP programmes. Debt management has improved during the term of the current government owing mainly to improved expertise.

Commentators suggested that the main problem in terms of transparency in Peru is not the lack of relevant legislation but rather loopholes in the laws and a lack of effective implementation.

Peru’s overall score is unchanged from last year.

1. CLARITY OF ROLES, RESPONSIBILITIES, AND OBJECTIVES



Enacted

The government sector should be distinguished from the rest of the public sector and from the rest of the economy, and policy and management roles within the public sector should be clear and publicly disclosed.

Peru has sustained the efforts to provide a sound legal framework to define and implement the structure, functions and responsibilities of the state, as established in the 1993 Constitution of Peru (as amended) and complementary legislation.¹ The decentralisation process -- aimed at redefining the government's functions and responsibilities -- has made progress over the past year.

Structure, functions and responsibilities of government

The government's structure and responsibilities are clearly defined in the constitution. The public sector is defined as the central government, the decentralised government, independent agencies and the autonomous branches of government. The central government includes the ministries and government agencies, while the decentralised government includes the regional and municipal governments, the independent regulatory agencies, the Office of the Comptroller General (CGR), the Central Reserve Bank of Peru (BCRP) and several state-owned enterprises.

Peru has traditionally been one of the most centralised governments in Latin America. Therefore, in recent years, the government has embarked on a comprehensive process of fiscal decentralisation.² In the past, some commentators had stated that the decentralisation process was poorly conceived, driven by political interests focused on financing social programmes without sunset clauses.³ Overall, the Law on the General Framework for Decentralisation appeared to establish an inadequate plan for fiscal and management procedures at all government levels.⁴

The Fiscal Decentralisation Decree (No. 955, enacted in February 2004) establishes several principles to provide incentives for regional and local governments to collect taxes, and to streamline the fiscal process for allocating transfers from national expenditure to these levels of government. Previously, some commentators had also expressed concern about the weakness in the Law on the General Framework for Decentralisation with regard to the requirement of reducing 25 regional governments to less than ten, since the process appeared technically challenging and politically unfeasible. The Law on Incentives for the Integration and Structuring of Regions (No. 28274, enacted in July 2004) and the Fiscal Decentralisation Decree provided a blueprint for regional integration through a referendum process.⁵ The referendum took place on 30 October 2005, when 16 of the 25 departments (regions) voted on whether or not to merge with neighbouring regions to create so-called macro-regions. Voting is obligatory, but commentators expressed doubt as to whether people understood what they were voting on.⁶ It was also noted by commentators that while the main incentive for supporting the mergers was that the new, larger regions would receive 50% of the taxes generated in the region, the bulk of the taxes are generated in Lima where most major companies are based, even if their productive facilities are based elsewhere.⁷ The result of the referendum was an overwhelming rejection of the merger proposal. Additional regulations to increase the efficiency of tax collection and to set up a certification system to verify regional/municipal governments' administrative capacity were issued during 2004.⁸

Nevertheless, the work of the National Decentralisation Council (CND), in charge of supervising the gradual process of transferring resources and responsibilities to regional and municipal governments -- mainly health and education

programmes and some public investment infrastructure projects -- is still perceived as being weak. The CND has had a history of having little success in generating consensus; its resolutions have been perceived as highly politicised and not representative of regional governments' interests.⁹

Over the past year there has been some progress in the area of decentralisation. In September 2005, the government issued the regulations implementing the Fiscal Decentralisation Law, which aims at reinforcing prudent budgetary practices of regional and local governments. The regulations aim to, *inter alia*, ensure that the assigning of resources to the regions is carried out in an orderly and gradual manner and they detail various incentives for the regions to use resources efficiently and in a fiscally responsible manner.¹⁰ A pilot programme is being established to foster regional and local government financial management capacity, including the development of multi-annual fiscal frameworks and capacity-building in project pre-investment procedures.¹¹ Finally, the law clarifying shared functional responsibilities among different levels of government (LOPE -- *Ley Organica de Poder Ejecutivo*) is currently before Congress. Commentators noted that efforts to replicate the national fiscal system at the local level are hindered by the continuing lack of technical capacity in many of the regions. It was suggested that in some cases the regions are receiving resources, but there is a lack of capacity to administer the money effectively as yet.¹²

Coordination and management of budgetary activities

The Ministry of Economy and Finance (MEF) controls the budget process.¹³ The MEF's Budget Office arranges the proposed budget documentation, which for the fiscal year 2005 includes the budget of the central government, decentralised institutions (including regional and municipal governments), and independent regulatory agencies (except for the Superintendence of Banking and Insurance -- SBS). State-owned enterprises administered by the National Fund for State Enterprise Activity (FONAFE), the BCRP, and the Social and Health Insurance Fund (ESSALUD) lie outside the budget law.

Relations between government and public sector agencies

The constitution establishes the independence of the BCRP, regulatory and supervisory agencies, and the Office of the Comptroller General (CGR). However, the current institutional arrangements do not fully guarantee this legal independence. In particular, the concurrence of tenures of BCRP board members and officials from the SBS with the presidential and legislative terms casts some doubts on the independence of the appointed officials in practice.¹⁴

Government involvement in the private sector

Public sector involvement in the private sector has been substantially reduced through privatisations and through operating concessions. Privatisation has stalled over the past year, however, and the government is now primarily restricting itself to operating concessions and conducting a limited number of public-private partnerships (PPPs). The most significant upcoming planned concession is for the Port of Callao, though this has been a controversial issue and the timing is unclear. This is likely to remain the case for the foreseeable future. *ProInversion* is the agency which manages privatisation, though commentators noted that it lacks the power to work effectively.¹⁵ Commentators expressed concern over the transparency of the costly Transoceanic Highway project (a highway connecting Peru and Brazil). This was presented as a PPP, though the government is ultimately going to bear the majority of the costs. Commentators stated that there was a lack of transparency in the management of the project, with regulations being circumvented and allegations of corruption. Commentators noted that there is a need for a clearer definition of what constitutes a PPP and perhaps even a law governing their framework to increase transparency.¹⁶

State-owned enterprises are regulated and managed by the FONAFE, an agency that lies under MEF jurisdiction.¹⁷ The FONAFE approves the annual budget of about 35 state-owned institutions, including financial public enterprises, utilities, and other energy and industrial enterprises.¹⁸

All FONAFE companies are subject to the provisions of the Law on Transparency and Access to Public Information 2002 (LTAIP). FONAFE makes publicly available the enterprises' financial statements on a consolidated basis.¹⁹ However, some concerns remain over the institutional framework that oversees the management of state-owned enterprises, with a consensus that more transparency and performance evaluation is needed.²⁰ The state-owned oil refining and commercialisation firm Petro Peru was regarded with particular concern by commentators.²¹

The public financial institutions -- COFIDE, *Banco de la Nacion*, and *Banco Agropecuario* -- are incorporated under FONAFE and are primarily governed by their own statutes; they do not normally engage in direct lending activities, except for public entities and public sector employees/pensioners. Although these are subject to SBS oversight, the absence of effective independence of the SBS president can also potentially increase fiscal risks.²²

There should be a clear legal and administrative framework for fiscal management

Peru's legal framework for fiscal management remains clear, although its fiscal responsibility framework, the approved fiscal deficit, and multi-annual budgeting rules have rarely been observed in the past. In May 2003, the Law on Fiscal Prudence and Transparency (No. 27245 -- LPTF) was modified through the Law on Fiscal Responsibility and Transparency (No. 27,958 -- LRTF),²³ since a number of fiscal ceilings of the LPTF had been broken. Legislation to complement the Law of Fiscal Responsibility and Transparency is due to be sent to Congress before the end of the year. This will aim to strengthen the procedures for compliance and monitoring, and the requirements for reporting to Congress and the public. Commentators described the law in its current state as lacking 'teeth', that is, sanctions for non-compliance, which has happened in some instances.²⁴ In addition, the General Law on the National System of Public Indebtedness (No. 28,112) provides a broad framework to review the financial administration of the public sector. It establishes basic rules for the efficient management of the processes linked to the collection and allocation of public resources, under the framework of fiscal responsibility and transparency as established by the LRTF.²⁵

In June 2005, the General Law on Public Indebtedness was passed. This aims to provide a stable legal framework to engender a more efficient and orderly administration of public sector indebtedness. It establishes rules on annual limits on debts and guarantees conducted through the central government, as well as on contingent liabilities stemming from concessions and public-private partnership programmes.²⁶

Legal framework for budgetary activities

The constitution requires the government to present an annual budget bill to Congress, in which no new expenses may be introduced. If Congress fails to approve the budget, the government may enact the budget bill by legislative decree.²⁷ The Law on Budget Management of the State of 1999 (No. 27,209 -- LBMS) governs the budget process, establishing technical criteria and budgeting procedures.²⁸ The LBMS centralises the budget process in the MEF's Budget Office, which collates budget projects of the different government agencies and arranges the national budget bill. Although these projects are required to follow strategic planning criteria and meet the objectives of the National Strategic Plan, in practice there is a weak link between the budget process and the general planning process.

The Budget Office has the authority to regulate the budget process, to design the annual disbursement programme, and to review budget execution to evaluate fiscal management and performance by government agencies. Some commentators have perceived the budget process in Peru as somewhat inefficient, and they have stressed that there has been no progress in introducing programme- and performance-based budgeting criteria.²⁹ The budget has usually been modified early in the fiscal year, which has generated considerable differences between the initial appropriations and the final disbursed expenses. Commentators noted that supplementary credits given mid-way

through the year, which are legally required as not all the funding is available at the time the budget is approved, are nevertheless a disincentive to spent efficiently.³⁰

The executive has considerable discretion to modify appropriations that are authorised by the LBMS, although further restrictions have been set up under the LRTF. In addition, commentators said that presidential Urgent Decrees to amend the budget, although frequently used in the past, are nevertheless illegal.³¹ Minor changes within a given appropriation may be carried out through resolutions issued by the government agency responsible for executing the expenses. Budget cuts do not require congressional approval; the vice-minister of finance approves them.

Together with the Annual Budget Bill, the administration submits the Financial Balance Bill and the Public Debt Bill (*Ley de Endeudamiento Publico*) for congressional approval. The Annual Budget Bill includes all the appropriations, while the Financial Balance Bill includes the financial plan for the balanced budget requirement. The lending bill requests congressional authorisation to carry out the lending programme established in the financial balanced budget plan. The three laws are presented to Congress through a *Statement of Objectives*, which sets out the assumptions and criteria used to forecast revenues and the overall economic objectives of the budget.³²

There are plans to unify the central government budget formulation system and the Integrated Financial Management System (SIAF). The challenge here is posed by the different classification systems currently used by the two systems. The government is also working on a system to prioritise budget items.³³

Legal framework for taxation

The constitution allocates authority to set taxes to Congress. Under congressional delegation, the executive branch can also set taxes through legislative decree. The executive has the authority to set taxation tariff rates through Supreme Decrees, but cannot introduce new taxes in emergency situations. The National Superintendence of Tax Administration (SUNAT) is responsible for tax collection and publishing tax laws, which are available on its website. With assistance from the Inter-American Development Bank, the government continues to expand financial administration and control systems for tax collection.

Substantial progress has been made in strengthening SUNAT's legal and institutional framework to reduce tax evasion. Administrative changes have increased tax collections. However, some commentators judged that there is a lack of reporting following the introduction of amendments or new taxes. For example, in 2003 Congress approved the controversial Financial Transactions Tax (ITB). The aim of the ITB was primarily to increase tax collection indirectly, by allowing all financial transactions to be registered for tax purposes, and thus making it easier to detect evasion of income and value-added tax.³⁴ There is a lack of publicly available analyses or assessment reports that explain what the benefits of the ITB and the detection of tax evasion have been to date.³⁵

Ethical standards for public servants

Ethical standards for civil servants are set out in the Code of Ethics of the Public Sector, which is publicly available and sets forth principles to guide the work and personal conduct of public officials.³⁶ The code is binding on all public sector employees, whether appointed to a regular civil service position, to a 'trust' (*confianza*) position, or to perform activities on behalf of the government.

2. PUBLIC AVAILABILITY OF INFORMATION



Compliance in progress

The public should be provided with full information on the past, current and projected fiscal activity of government.

Peru remains committed to the IMF Special Data Dissemination Standards (SDDS), with which it largely complies despite a few exceptions -- the *Boletín de Transparencia*, for example, does not comply fully with SDDS requirements and there is a lack of advance release calendars. Efforts are underway to fully comply with SDDS, but a lack of appropriate infrastructure constrains full implementation at this stage.³⁷ The constitution recognises the right of all citizens to access adequate government information. The LTAIP further develops this concept.³⁸ In compliance with these rules, Peru publishes a wealth of information on fiscal activity, available on the MEF's website.³⁹ Fiscal data is published in the monthly *Fiscal Transparency Newsletter* (Boletín de Transparencia Fiscal - BTF), which also compiles reports on relevant issues and publishes data that is not available on a regular basis.⁴⁰

The LPTF requires the government to disclose its medium-term economic and fiscal policy objectives in the Multi-Annual Macroeconomic Framework (*Marco Macroeconómico Multianual* -- MMM). The MMM is published at the beginning of June each year, together with a technical opinion from the BCRP and a subsequent revision (made if some of the underlying assumptions change significantly).⁴¹

Central government operations

The MEF reports monthly on the central government's fiscal performance in the BTF. In addition to these reports, a detailed execution of the budget is available from the Integrated System of Financial Administration of the Public Sector (SIAF-SP).⁴² The system includes information that compares the monthly cash disbursement and fiscal execution by government agency and programme.

Public sector operations

The MEF reports quarterly on the decentralised public sector, which includes the regional and local governments as well as other government agencies and non-financial public enterprises. The government provides reports on the fiscal activity of the consolidated public sector within 90 days of the end of the fiscal year, including financial public enterprises and the BCRP. The MEF's *Economic Transparency* website also posts fiscal information on macroeconomic projections, sectoral management and budget execution plans, and budget information by government agency.

Important progress has been achieved in connecting regional and local governments in order to collate fiscal data. Commentators said that at present only statistics on external debt and overall expenditure are up to date. Nevertheless, municipalities are being involved in applying the SIAF system (currently used in approximately 1,300 of the 1,800 municipalities) in order to improve the accuracy of their accounting records and enhance the availability of procurement data.⁴³ Some commentators suggested that the limited technical capacity of the municipalities has been a problem in some cases thus far when applying the SIAF system.⁴⁴

Public financial institutions conduct some quasi-fiscal operations. *Banco de la Nación* provides loans to the government, public entities, and public sector employees/pensioners at preferential interest rates; *Banco*

Agropecuario extends direct loans to small farmers at preferential rates funded by the treasury, as well as indirect loans through private financial institutions. More recently, the BCRP has been carrying out quasi-fiscal activities by purchasing substantial amounts of dollars in the foreign exchange market and then issuing bonds (short-term Certificates of Deposit) to reduce the liquidity of the domestic currency in the financial system (sterilisation). Commentators stated that, although the associated costs are manageable, additional information on BCRP interventions would enhance overall transparency.⁴⁵

A commitment should be made to the timely publication of fiscal information.

Article 22 of the LTAIP requires all government agencies to publish budgets, public investment projects with their level of execution, information on personnel, and public management assessment indicators on a quarterly basis. Article 23 requires the MEF to publish the consolidated public sector balance (including public financial institutions and other entities outside the annual budget) within 90 days of the end of the fiscal year. The LTAIP also mandates quarterly releases of public debt and fiscal sustainability information, contingent liabilities, and disclosure of fiscal risks.

Debt reporting

The MEF's Public Credit Office publishes an internal report on government debt and lending operations including offers of domestic and foreign bonds, and information on the repayment schedules and debt servicing for the fiscal year and maturities and debt stocks. Information is also grouped by currency denomination and type of lending mechanism. In the publicly available *Boletín de Transparencia*, there is information on internal and external debt and the financing of that debt, though not in the detail found in the internal report. The MEF's *Economic Transparency* website also publishes debt information, although, again, this is not as detailed as data in the internal report by the Public Credit Office. The BCRP also reports public and private debt data.

Important progress in providing information on pension liabilities and other contingent liabilities has been made in the last two years. The government is working on improving the reporting of public sector liabilities associated with public-private partnerships (PPPs). There is a registry of contingent guarantees held by the MEF's Public Credit Office, though this is not publicly available. There are also limits set in law annually on the guarantees the government can give for PPPs.⁴⁶

In recognition of the threat that pension liabilities will represent in the future, the government has reformed the constitutional provisions with regard to the '20530' (also known as *cedula viva*) pensions regime, such that employees cannot join under the original benefits scheme.⁴⁷ A cap was also put on those pensions currently held under the *cedula viva* scheme, to around \$2,000 US dollars a month, by reducing them by 18% per year. This was approved under the constitutional reform to the *cedula viva*, though there has been talk of some Congressmen proposing a law amending the constitutional amendment to make a reduction of 18% only on the excess over \$2,000 US dollars. This looks unlikely to pass.⁴⁸ Further improvements on reporting contingent liabilities stemming from the pensions system, such as the *bonos de reconocimiento* -- the lump-sum payment made when a worker moves from the public pension system into a private one (AFPs) -- is also in progress.⁴⁹ The *bonos de reconocimiento* are now reflected in the MMM.⁵⁰ In December 2004, the government agreed to reform the pension regimes of the police and military, though commentators noted that this is at a very early stage of discussions and the government is considering various options.⁵¹

Advance release calendars

The MEF does not make available an advance release calendar for central government and public sector data, although a calendar can be found on the IMF SDDS website.⁵²

3. OPEN BUDGET PREPARATION, EXECUTION AND REPORTING

●●●● Compliance in progress

Fiscal policy objectives, macroeconomic framework and risks

Government agencies submit their budget proposals to the MEF's Budget Office. The Law on Budget Management of the State (LBMS) requires all government agencies to frame the budgeting process within multi-annual strategic plans but, in practice, this has rarely occurred. The MEF's Office of Multi-Annual Planning is responsible for ensuring that government agencies follow multi-annual strategic plans; to this end the office has issued a series of standard guidelines and regulations. In addition, the MEF's Budget Office issues a series of directives that aim to improve the relationship between the planning process and budgeting of expenses and revenues. Although the Budget Office and several government agencies have signed management agreements to introduce performance-based budgeting, commentators have reported only minor progress in this area.

Last year's budget incorporated the input from regional governments for the first time; a process that has been repeated for the fiscal year 2005 and 2006 budgets. This step is aimed at boosting the fiscal decentralisation process by transferring social expenditure responsibilities with support from all levels of government.⁵³

Fiscal policy objectives

The budget's *Statement of Objectives* contains the annual fiscal objectives and explains how the budget bill intends to meet its targets, as established in the MMM. Some commentators asserted that, unlike in previous years, many of the objectives established in the MMM were now being met. In particular, the strengthened macroeconomic stability -- in addition to more comprehensive analyses of long-term debt sustainability and economic scenarios -- has reduced the need to substantially revise the underlying assumptions. This has allowed for a more robust assessment of how medium-term targets are being met through short-term changes in fiscal policy.⁵⁴

Macroeconomic framework

The public sector budget is linked to the objectives established in the MMM, although a multi-annual budget is not in place in Peru -- only the budget for the pertinent fiscal year is enacted. The annual fiscal process thus follows the underlying MMM, which covers the fiscal year and the following two years. The MMM includes a series of fiscal principles and objectives, forecasts of revenues and expenses, and the assumptions used to formulate the plan. The Office of Fiscal Affairs produces a follow-up report.⁵⁵

Fiscal risks

For fiscal year 2006, the *Statement of Objectives* and the budget bill include a brief explanation of the main fiscal risks. There are well-established assumptions in the budget statement about growth, inflation, exchange rate levels and interest rates. The government has started a comprehensive process of project feasibility, coordinated between the SIAF-SP and the National System of Public Investment (SNIP), under which any public sector project will need to incorporate a feasibility study as a requirement for approval. However, in order to successfully quantify (and reduce) fiscal risks, stronger efforts on project monitoring should be implemented since, historically, many regional projects have become unprofitable after a number of years of operation, forcing the government to provide substantial subsidies.⁵⁶

Fiscal sustainability

In April 2003, the MEF made available a special report on fiscal sustainability (included in a BTF) for 2003-13.⁵⁷ The analysis incorporates the impact of the latest changes in fiscal policy and overall macroeconomic outcomes as established in the MMM 2004-06.

Article 4 of the LRTF establishes that the MMM must include an analysis of fiscal sustainability. In agreement with this provision, the 2004 and 2005 MMMs include a fiscal sustainability analysis, and the MMM 2005-07 includes an analysis of public debt sustainability and sensitivity scenarios of the medium-term fiscal outlook.⁵⁸

Budget presentation

Budget presentation has improved over the past couple of years; the 2005 budget draft contained additional information, disaggregated by programme and function, which was previously not available, and thus helps to provide an assessment of economic impact. However, some commentators still judged both the practices and statutory requirements for the link between budget allocation and the subsequent reporting of each programme's achievements as too weak.⁵⁹ This year's budget again includes spending execution and agency targets for the previous year, and makes an effort to establish a clear relationship between the annual budget and the MMM 2005-07.

Data reporting

SDDS data on the general government operations are recorded in gross terms, except lending for policy purposes, which is recorded net of payments. The classification of revenues, expenditures and financing largely complies with the requirements of the IMF's Government Financial Statistics Manual. However, while expenditures are recorded with accrual-based accounting, revenues are recorded using cash-based accounting. Expenditures of the general government are organised by economic classification, divided into current and capital expenditure. Peru includes a classification of expenditures by function in the annual budget by priority public expenditure areas. The General Department of Social and Economic Affairs lists these areas and provides monthly functional reporting on social programmes.

Budget execution and monitoring

The SIAF-SP follows up budget execution by central government agencies and a number of regional budgets and projects. The system monitors budget execution electronically and its reports are available on the MEF website. The information includes the annual budget appropriation and the accumulated execution as well as the amounts programmed for execution during any given month. However, the IMF has identified a number of shortcomings in the operational design and accounting practices of the SIAF, in particular regarding the adequate monitoring of payment arrears in a reliable way.⁶⁰

Accounting basis

The National Accounting Office defines, enforces and evaluates the accounting systems for institutions under the public sector budget. Peru follows a dual system that registers income on a cash-basis and expenses on an accrual-basis. As a result, there are considerable budgetary lags, and treasury disbursements are often made effective outside the scheduled dates. Commentators said that these problems are clearly observed by the end of the fiscal year, as a number of sub-national government departments spend up to 20% of their budget near the end of the year.⁶¹

Procurement and employment

The government's Supreme Council for Government Contracting and Acquisitions (CONSUCODE) administers the national register of contractors, and sets out guidelines for procurement. By law, government agencies must provide quarterly reports to the CONSUCODE and the CGR on their procurement practices. However, the procurement process in Peru is still considered inefficient, with low transparency in acquisitions and considerable bottlenecks in the decision-making process. CONSUCODE is currently developing a process of electronic procurement (*Peru Contrata*) integrated to the SIAF-SP, which will allow for transparent publication of procurement decisions and bidding procedures.

According to the IMF, procedures for hiring and remunerating government personnel have been found to be opaque and open to discretion. Fewer than half the workers in the executive branch are career civil servants, and the variety of personnel regimes and remuneration schemes are subject to different principles, criteria, and standards.⁶² In 2003, a census on the number of public workers and pensioners was concluded; it covered the national government, regional governments, military personnel, non-personal services' contracts and others. The census is now complete, but it has not been made public, and for reasons of confidentiality there are no plans to do so. Commentators stressed, however, that it would be useful to make the principal findings of the census public.⁶³

Fiscal reporting

The MEF submits two reports every year to Congress, in compliance with the LRTF. These reports set out the progress made in achieving the fiscal policy goals stipulated in the MMM and the budget law, and record any budget cuts. The reports are available on the MEF's website and from its press office. Trimestal reports on projections are also published and are available on the MEF website.

4. ACCOUNTABILITY AND ASSURANCES OF INTEGRITY



Enacted

Data quality standards

The BCRP collates national macroeconomic statistics and data, in line with the IMF SDDS. The MEF and the BCRP, through the SIAF-SP system, verify the internal consistency of fiscal information. Both institutions present quarterly fiscal information with broad coverage of the non-financial public enterprises and the general government (which includes the consolidated central government and local governments covering approximately 90% of total municipalities), with a lag of about five weeks and in agreement with the LRTF.

Independent scrutiny of fiscal information

The Office of the Comptroller General (CGR), an autonomous entity that exercises external control over the public sector, supervises the execution of the budget, public debt management and the activities of public sector institutions. The CGR may also introduce measures for internal control, and exercise ex post external control directly, or contract an external audit firm through competitive bids to conduct external audits of public sector agencies if these are in a position to cover the underlying costs. After being in disrepute for its lack of independence and control over fiscal execution during the 1990s, the CGR has been undergoing a process of reform. In 2002, an Organic Law on the Office of the Comptroller General was approved, which substantially strengthened its auditing powers.⁶⁴

In 2004, commentators said that some progress was achieved in solving the office's serious problems of underfunding and lack of human and technical resources. Nevertheless, doubts remain about its independence over auditing and monitoring of public expenditure, and about the actual follow-up and actions that public sector agencies perform as part of CGR's recommendations -- even though the CGR has powers to impose sanctions for non-compliance. Indeed, the lack of public sector accountability is perceived as one of the most serious problems in the country.⁶⁵

Independent Audit

The government has internal and external auditing procedures. Control offices carry out internal auditing, while the CGR exercises external control activities. However, the shortage of resources could potentially hamper the capabilities of the CGR to effectively audit fiscal accounts, budgetary execution, and management of public resources at all government levels.⁶⁶ The CGR is under congressional oversight, on the basis of an annual report prepared by the Comptroller General, who is appointed by Congress for a term of seven years. The CGR's audit practices are consistent with the standards of the International Organization of Supreme Audit Institutions (INTOSAI).

National Statistics Agency

The central statistics organisation in Peru is the National Institute of Statistics and Data Processing (INEI).⁶⁷ The INEI is an independent institution; its website outlines the methodologies employed and its scope of activity. The INEI uses fiscal data to prepare national accounts.

INTERVIEWS

Representatives of *Oxford Analytica* interviewed the following individuals during a visit to Peru between 19 and 21 October 2005:

Ministry of Economy and Finance

21 October 2005

Javier Kapsoli
Briggit Bencich

Economic and Social Affairs
Economic and Social Affairs

Central Reserve Bank of Peru (BCRP)

19 October 2005

Jorge Estrella Viladegut
Fernando Herrada

Deputy Director of the Public Sector

Economic Studies Department
Economic Studies Department

ADDITIONAL INTERVIEWS

19 October 2005

Eduardo Moron

Macroeconomics and Political
Economy Area

Centro de Investigacion
Universidad del Pacifico

20 October 2005

Elmer Cuba

Chief Economist

Macroconsult

21 October 2005

Mario Alberto Guerrero Corzo
Daniel Cordova Espinoza

Senior Analyst, Economic Studies
Analyst, Economic Studies

Banco Wiese, Sudameris
Banco Wiese, Sudameris

Enrique Cornejo

Chief Adviser and
National Director -- Economics

APRA Parliamentary Desk
Partido Aprista Peruano

NOTES

¹ The 1993 Constitution of Peru (in Spanish only): www.leyes.congreso.gob.pe/Imagenes/Constitu/Cons1993.pdf

² See for example 'IADB Program of Modernization and Decentralization of the State in Peru' PE-0217 (2002). Profile II www.iadb.org/exr/doc98/pro/upe0217.pdf

³ Interviews in Peru, 18-20 November 2003.

⁴ Interviews in Peru, 18-20 November 2003. See *Ley de Bases de Descentralización*, Law 27,783 of 2002 (in Spanish only): www.leyes.congreso.gob.pe/Imagenes/Leyes/27783.pdf

⁵ See the *Law on Incentives for the Integration and Structuring of Regions* (in Spanish only) at: www.congreso.gob.pe/ntley/Imagenes/Leyes/28274.pdf The *Fiscal Decentralisation Decree* (in Spanish only) is at: www.congreso.gob.pe/ntley/Imagenes/DecretosLegislativos/00955.pdf

⁶ The defeat of the regionalisation initiative will increase frustration and suspicion of Lima in the provinces and may hamper future attempts to form larger units. If these attempts are to have a chance of success, they will have to include a far greater degree of citizen participation in the planning process. Oxford Analytica Daily Brief, 'Regionalisation Rejected in Referendum', 2 November 2005.

⁷ Interviews in Peru, 19-21 October 2005.

⁸ See, for example, 'Ley de Sistema de Acreditación de los Gobiernos Regionales y Locales' (in Spanish only): www.congreso.gob.pe/ntley/Imagenes/Leyes/28273.pdf

'Decreto Legislativo que Modifica el Decreto Legislativo No. 776, Ley de Tributación Municipal' (in Spanish only): www.congreso.gob.pe/ntley/Imagenes/DecretosLegislativos/00952.pdf

⁹ Interviews in Peru, 17-19 November 2004.

¹⁰ Interviews in Peru, 19-21 October 2005.

¹¹ IMF, Peru -- Letter of Intent, Memorandum of Economic and Financial Policies, and Technical Memorandum of Understanding, 20 May 2005 and interviews in Peru, 19-21 October 2005.

¹² Interviews in Peru, 19-21 October 2005.

¹³ Ministry of Economy and Finance (*Ministerio de Economía y Finanzas*): www.mef.gob.pe

¹⁴ Interviews in Peru, 18-20 November 2003.

¹⁵ Interviews in Peru, 19-21 October 2005.

¹⁶ Interviews in Peru, 19-21 October 2005.

¹⁷ *National Fund for State Enterprise Activity* (FONAFE): www.mef.gob.pe/fonafe01.htm

¹⁸ For a list of incorporated enterprises (in Spanish only): www.fonafe.gob.pe/empresas.asp

¹⁹ See financial information by enterprise (in Spanish only) at: www.fonafe.gob.pe/infocinanciera.asp

²⁰ Interviews in Peru, 17-19 November 2004.

²¹ Interviews in Peru, 19-21 October 2005.

²² Interviews in Peru, 18-20 November 2003.

²³ *Ley que Modifica la Ley 27,245 de Prudencia y Transparencia Fiscal*, Law 27,958 of 2003 (in Spanish only): www.leyes.congreso.gob.pe/Imagenes/Leyes/27958.pdf

²⁴ IMF, Peru -- Letter of Intent, Memorandum of Economic and Financial Policies, and Technical Memorandum of Understanding, 20 May 2005 and interviews in Peru, 19-21 October 2005.

²⁵ *Ley Marco de la Administración Financiera del Sector Público*, Law 28,112 of 2003 (in Spanish only): www.leyes.congreso.gob.pe/Imagenes/Leyes/28112.pdf

²⁶ IMF, Peru -- Letter of Intent, Memorandum of Economic and Financial Policies, and Technical Memorandum of Understanding, 20 May 2005 and interviews in Peru, 19-21 October 2005.

²⁷ Articles 78-80 of the constitution.

²⁸ *Ley de Gestión Presupuestaria del Estado*, Law 27,209 of 1999 (in Spanish only): www.leyes.congreso.gob.pe/Imagenes/Leyes/27209.pdf

²⁹ Interviews in Peru, 17-19 November 2004. See Rossana Mostajo Guardia (2002), 'El Sistema Presupuestario en el Perú', ILPES Serie Gestión Pública No. 17. CEPAL at: www.eclac.org/publicaciones//4/LCL1714P/sgp17.pdf

³⁰ Interviews in Peru, 19-21 October 2005.

³¹ Interviews in Peru, 18-20 November 2003. For example, between 1993 and 2000, the government issued 1,003 Urgent Decrees that increased spending by over one billion US dollars. See Mostajo Guardia (2002) p. 19.

³² See *Proyectos de Ley -- Año Fiscal 2005* (in Spanish only): <http://transparencia-economica.mef.gob.pe/documento/default4.asp>

³³ IMF, Peru -- Letter of Intent, Memorandum of Economic and Financial Policies, and Technical Memorandum of Understanding, 20 May 2005 and interviews in Peru, 19-21 October 2005.

³⁴ Interviews in Peru, 18-20 November 2003. A number of commentators expressed concern about potential ‘side effects’ stemming from the implementation of the ITB. For example, even though the 0.15% rate is very low, there could be serious financial distortions should it discourage people from using the financial system. This might hamper financial intermediation and/or might result in people transferring money to other countries.

³⁵ Interviews in Peru, 17-19 November 2004.

³⁶ *Ley del Código de Ética de la Función Pública*, Law 27,815 of 2002 (in Spanish only):

www.leyes.congreso.gob.pe/Imágenes/Leyes/27815.pdf

³⁷ IMF Special Data Dissemination Standard Site (SDDS) at: <http://dsbb.imf.org> Interviews in Peru, 19-21 October 2005.

³⁸ *Ley de Transparencia y Acceso a la Información Pública* (LTAIP), Law 27,806 of 2002 (in Spanish only):

www.leyes.congreso.gob.pe/Imágenes/Leyes/27806.pdf

³⁹ Interviews in Peru, 18-20 November 2003. Commentators said that the general presentation of fiscal data has been made substantially more ‘user friendly’ than before. See for example the *Economic Transparency* website of the MEF at: <http://transparencia-economica.mef.gob.pe>

⁴⁰ Boletín de Transparencia Fiscal (BTF, in Spanish only):

<http://transparencia-economica.mef.gob.pe/documento/default2.asp>

⁴¹ See, for example, *Marco Macroeconómico Multianual 2005-2007* (in Spanish only):

<http://transparencia-economica.mef.gob.pe/proyeccion/multianual.asp>

⁴² SIAF-SP at: www.mef.gob.pe/siaf/

⁴³ Interviews in Peru, 18-20 November 2003. The SIAF now has about 60 officials based around the country to introduce the SIAF in the municipalities.

⁴⁴ Interviews in Peru, 19-21 October 2005.

⁴⁵ Interviews in Peru, 17-19 November 2004.

⁴⁶ Interviews in Peru, 19-21 October 2005.

⁴⁷ For example, the *cedula viva* pension regime gave retired public sector employees a pension equivalent to the salary of the official who currently held the job. In addition, pensions were transferable to the spouse (after the employee’s death) and from the spouse to a daughter (conditional on the daughter remaining single). See *Régimen de Pensiones y Compensaciones por Servicios Civiles prestados al Estado no comprendidos en el Decreto Ley 19990* (Law No. 20530 of 1974) at: www.congreso.gob.pe/ntley/Imágenes/Leyes/20530.pdf

⁴⁸ Interviews in Peru, 19-21 October 2005. The reform of the constitutional provisions on the *cedula viva* also ended the so-called ‘mirror effect’ which had meant that the government was discouraged from raising the salaries of public employees because it would then have to raise the pensions of all those retired employees who had held that position.

⁴⁹ Interviews in Peru, 17-19 November 2004. The central bank has a special reserve of two billion US dollars (from privatisation revenues) that is solely used for issuing *bonos de reconocimiento*. In the MMM 2005-2007, and in agreement with IMF fiscal accounting standards, the financial requirements for the *bonos de reconocimiento* were reclassified as internal debt servicing (‘below-the-line’ expenditures), instead of ordinary government expenses (‘above-the-line’). See *Anexo A -- Cambios en la Contabilidad de la Redención de los Bonos de Reconocimiento* (in Spanish only) at: http://transparencia-economica.mef.gob.pe/proyeccion/doc/MMM2005_2007.pdf

⁵⁰ Interviews in Peru, 19-21 October 2005.

⁵¹ IMF, Peru -- Letter of Intent, Memorandum of Economic and Financial Policies, and Technical Memorandum of Understanding, 20 May 2005 and interviews in Peru, 19-21 October 2005.

⁵² IMF SDDS, Peru, advance release calendar: <http://dsbb.imf.org/Applications/web/sddsctycatarelist?strcode=PER>

⁵³ Interviews in Peru, 18-20 November 2003.

⁵⁴ Interviews in Peru, 17-19 November 2004.

⁵⁵ Follow-up report of *Marco Macroeconómico Multianual 2003-2005* (first half 2003, in Spanish only):

http://transparencia-economica.mef.gob.pe/proyeccion/doc/Informe_Seguimiento MMM2003_2005_ISem2003.pdf

⁵⁶ Interviews in Peru, 17-19 November 2004.

⁵⁷ <http://transparencia-economica.mef.gob.pe/propuest/DGAES/btfiscal/N21BTFInforme.pdf>

⁵⁸ See MMM, Section 5.2 *Dinámica de la Deuda y Sostenibilidad* and Section 5.3 *Análisis de Sensibilidad* (in Spanish only) at: http://transparencia-economica.mef.gob.pe/proyeccion/doc/MMM2005_2007.pdf

⁵⁹ Interviews in Peru, 17-19 November 2004.

⁶⁰ See ‘Peru: Report on the Observance of Standards and Codes – Fiscal Transparency Module’, Country Report No. 04/109, April 2004, at: www.imf.org/external/pubs/ft/scr/2004/cr04109.pdf

⁶¹ Interviews in Peru, 18-20 November 2003. This problem is exacerbated by the fact that any funds that are not spent during the fiscal year might be subtracted from the budgeted amounts for the next fiscal year.

⁶² See 'Peru: Report on the Observance of Standards and Codes – Fiscal Transparency Module', Country Report No. 04/109, April 2004, at: www.imf.org/external/pubs/ft/scr/2004/cr04109.pdf

⁶³ Interviews in Peru, 19-21 October 2005.

⁶⁴ See *Ley Orgánica del Sistema Nacional de Control y de la Contraloría General de la Republica* (No. 27785, in Spanish only) at: www.congreso.gob.pe/ntley/Imagenes/Leyes/27785.pdf

⁶⁵ Interviews in Peru, 17-19 November 2004.

⁶⁶ Interviews in Peru, 18-20 November 2003.

⁶⁷ See www.inei.gob.pe